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Note by the Secretary-General

The Secretary-General has the honour to transmit herewith to the Security Council the report of the United Nations Board of Auditors on the United Nations escrow (Iraq) accounts for the biennium ended 31 December 2007.

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Report of the Board of Auditors on the audit of the United Nations escrow (Iraq) accounts established under the provisions of Security Council resolutions 687 (1991), 706 (1991), 778 (1992), 986 (1995), 1284 (1999) and 1483 (2003) for the biennium ended 31 December 2007

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Letter dated 31 March 2008 from the Secretary-General to the Chairman of the United Nations Board of Auditors

In accordance with financial regulation 6.5, I have the honour to submit the accounts of the United Nations escrow accounts established pursuant to Security Council resolutions 687 (1991), 706 (1991), 778 (1992), 986 (1995), 1284 (1999), 1483 (2003) and 1762 (2007) for the biennium 2006-2007, which I hereby approve. The financial statements have been completed and certified as correct by the Controller.

(*Signed*) **Ban** Ki-moon

I. Report of the Board of Auditors

Summary

The United Nations Board of Auditors has audited the financial statements of the United Nations escrow (Iraq) accounts, established under the provisions of Security Council resolutions relating to Iraq, for the biennium ended 31 December 2007. The audit was carried out through a review of the financial transactions covering the fourth year of the phase-down operations, taking into account the audit assurance obtained when the Board expressed an opinion on the 2006 financial statements of the escrow (Iraq) accounts. The financial statements of the escrow accounts are presented in accordance with the liquidation basis of accounting as a result of Security Council resolution 1483 (2003), by which the Council terminated the operations of the programme effective 21 November 2003.

The Board issued an unqualified opinion on the financial statements for the period under review, as reflected in section III.

Implementation of previous recommendations

In response to the request of the Advisory Committee on Administrative and Budgetary Questions and in line with paragraph 7 of General Assembly resolution 59/264 A, the Board evaluated the ageing of its previous recommendations that had not yet been fully implemented and has indicated the financial periods in which such recommendations were first made.

Of the seven recommendations contained in the Board's reports for the biennium ended 31 December 2005 and for the financial year ended 31 December 2006, two were implemented, four were under implementation as they required structured periodic action by the Administration, and one was overtaken by Security Council resolution 1762 (2007), by which the Council terminated the mandate of the United Nations Monitoring, Verification and Inspection Commission (UNMOVIC).

The Board noted the Administration's prompt implementation of its recommendation to prepare the financial statements of the United Nations escrow (Iraq) accounts in accordance with the liquidation basis of accounting, and the significant progress made in accelerating the wind-down and final closure of the programme.

The details of the implementation of previous recommendations are indicated in the annex to the present section.

Financial overview

As the programme is under liquidation, 62 per cent or $100.6 million of the total income was derived from interest on cash and term deposits and the cash pool. The cash pool was maintained to cover claims for outstanding obligations and other liquidation expenses.

Total income was $162.6 million, compared with $255.8 million for the previous biennium. The 36 per cent decrease was primarily attributable to the transfers made to the Development Fund for Iraq, amounting to $371.1 million. Total expenditure amounted to $118 million, compared with $421.5 million for the previous biennium, a decrease of 72 per cent. This resulted in an excess of income over expenditure of $44.6 million, compared with a deficit of $165.7 million in the preceding biennium.

The total cash resources of $1 billion adequately covered the $657.5 million in current and prior period unliquidated obligations arising from approved contracts for humanitarian supplies and oil spares. Total reserves and fund balances increased by 40 per cent, or $111 million, from $277 million in 2005 to $388 million in 2007. The increase was principally brought about by the excess of income over expenditure of $44.6 million and the increase in operating reserves of $60 million.

Wind-down and liquidation implementation

The slow issuance of authentication documents by the Government of Iraq and the protracted cancellation of letters of credit with no claims of delivery continued to hamper the complete liquidation and closure of the programme and the final transfer of the unencumbered cash balance to the Development Fund for Iraq.

Write-offs and disposals

The Administration had written off property losses amounting to $1.4 million and disposed of properties valued at $5.4 million.

Recommendation

The Board has made one recommendation arising out of its audit. This relates to the release of cash collaterals associated with the expired letters of credit with no claims of delivery.

A. Mandate, scope and methodology

1. The Board of Auditors has audited the financial statements of the United Nations escrow (Iraq) accounts established under the provisions of Security Council resolutions 687 (1991), 706 (1991), 778 (1992), 986 (1995), 1284 (1999), 1483 (2003) and 1546 (2004). Following the adoption of Security Council resolution 1483 (2003), the oil-for-food programme was terminated on 21 November 2003. The Secretary-General envisaged a timetable of up to the end of 2007 to complete the liquidation of the programme.

2. The audit was conducted in conformity with article VII of the Financial Regulations and Rules of the United Nations and the annex thereto, as well as the International Standards on Auditing. Those standards require that the Board plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement.

3. The audit was conducted primarily to enable the Board to form an opinion as to whether the financial statements presented fairly the financial position of the United Nations escrow (Iraq) accounts as at 31 December 2007 and the results of operations and cash flows for the financial period then ended in accordance with the United Nations system accounting standards. This included an assessment as to whether the expenditures recorded in the financial statements had been incurred for the purposes approved by the governing bodies and whether income and expenditures had been properly classified and recorded in accordance with the United Nations Financial Regulations and Rules. The audit also included a general review of financial systems and internal controls and a test examination of the accounting records and other supporting evidence to the extent that the Board considered necessary to form an opinion on the financial statements.

4. In addition to the audit of the accounts and financial transactions, the Board reviewed the extent to which the liquidation of the United Nations escrow (Iraq) accounts, mandated under Security Council resolution 1483 (2003), had been carried out. This matter is addressed in paragraphs 17 to 19 below.

5. The present report covers matters that, in the opinion of the Board, should be brought to the attention of the Security Council. The Board's observations and conclusions were discussed with the Administration, whose views have been appropriately reflected in the report.

B. Detailed findings and recommendations

1. Follow-up of previous recommendations

6. The Board reviewed the measures taken by the Administration to implement the four recommendations made in its report for the biennium ended 31 December 2005 (S/2006/673). One of the recommendations was implemented, two were under implementation, and one was overtaken by events. In addition, one of the three recommendations made in its report for the financial year ended 31 December 2006 (S/2007/445) was implemented, and two were under implementation. Details of the actions taken and the comments of the Board are presented in the annex to the present section.

2. Status of the oil-for-food programme

7. In 2007, the liquidation of the oil-for-food programme was in its fourth year of operation. As in the previous three years, all obligations relating to contracts that had not been prioritized in accordance with Security Council resolution 1483 (2003) had been closed except those associated with letters of credit that had pending claims of delivery. Obligations relating to contracts that had been prioritized remained as liabilities of the oil-for-food programme, and the related letters of credit have not been closed. The expiry dates for the letters of credit extended only until 31 December 2007. In his letters dated 10 July 2006 (S/2006/510), 8 December 2006 (S/2007/46), 27 March 2007 (S/2007/241), 25 July 2007 (S/2007/476) and 7 December 2007 (S/2007/725), the Secretary-General has kept the Security Council informed of the continuing arrangements for the liquidation of the outstanding letters of credit, and the very slow progress being made.

8. Through his letter dated 7 December 2007 (S/2007/725), the Secretary-General, inter alia, updated the Security Council on the extension and/or reinstatement of specific letters of credit; the submission to the designated bank of all the necessary documents related to the 17 letters of credit included in annex VI to the letter dated 25 July 2005; and the proposals to address unresolved issues, including the establishment of mechanisms to deal with outstanding issues. The Council has taken note of the matter and, through the letter dated 29 February 2008 from the President of the Council to the Secretary-General (S/2008/140), called upon the Working Group, composed of representatives from the Secretariat, the Central Bank of Iraq and the relevant ministries of the Government of Iraq, to continue its efforts expeditiously to resolve all outstanding issues. The President stated in his letter that the Council would further consider the procedures to be adopted by the Secretariat and the Government of Iraq to ensure the appropriate conclusion of the programme.

9. The Secretary-General reported, in his letter of 23 January 2008 (S/2008/41) to the President of the Security Council, that there were 210 outstanding letters of credit as at 31 December 2007 with an approximate value of $656.3 million. That number was reduced to 167, with an approximate value of $605 million, as at 29 February 2008 (S/2008/175). The decline was attributable to the cancellation of 40 letters of credit valued at $48 million and the payment in full of three letters of credit with an approximate value of $9.5 million.

10. The Board reviewed on a sample basis the completeness and validity of the authentication documents submitted to the United Nations by the Central Bank of Iraq for 2007. Statement I in section IV below reflects total expenditure of $118 million for the biennium 2006-2007. Of that amount, $88 million pertained to humanitarian activities and $83 million thereof remained unliquidated as at 31 December 2007. From the inception of the programme up to 31 December 2007, total expenditure for humanitarian supplies and oil spares reached $43.9 billion, as shown in table 1.

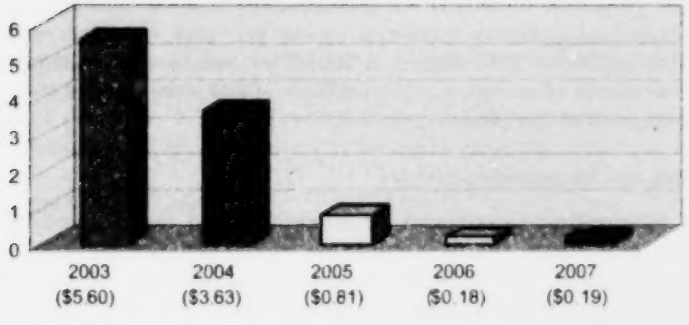
Table 1
Expenditures for humanitarian supplies and oil spares
(Thousands of United States dollars)

Biennium	*Humanitarian supplies*	*Oil spares*	*Total*
1996-1997	2 401 843		2 401 843
1998-1999	6 026 701	344 687	6 371 388
2000-2001	19 988 807	2 368 641	22 357 448
2002-2003	11 119 750	1 286 236	12 405 986
2004-2005	200 358	79 387	279 745
2006-2007	86 554	1 701	88 255
Total	**39 824 013**	**4 080 652**	**43 904 665**

3. Development Fund for Iraq

11. The Development Fund for Iraq was established pursuant to Security Council resolution 1483 (2003) of 22 May 2003, which mandated, inter alia, that unencumbered funds from the oil-for-food programme be transferred to it. For the biennium 2006-2007, a total of $371.1 million was transferred to the Fund and charged against the "Humanitarian activities in Iraq" account ($306.1 million) and the "Monitoring, verification and inspection" account ($65 million). As shown in figure I, from the adoption of Security Council resolution 1483 (2003) up to 31 December 2007, total transfers to the Development Fund for Iraq amounted to $10.41 billion. The Board's mandate does not include auditing of the activities or financial records of the Development Fund for Iraq.

Figure I
Funds transferred to the Central Bank of Iraq/Development Fund for Iraq
(Billions of United States dollars)



4. Financial overview

12. The significant account balances reflected in statements I and II (see sect. IV below) are set out in table 2.

Table 2
Analysis of account balances
(Thousands of United States dollars)

Account	*Biennium ended 2005*	*Biennium ended 2007*	*Increase (decrease)*	*Percentage increase (decrease)*
Total income	255 759	162 592	(93 167)	(36)
Total expenditures	421 492	117 954	(303 538)	(72)
Interest income (included in total income)	166 805	100 612	(66 193)	(40)
Humanitarian supplies and oil spares	279 745	88 255	(191 010)	(68)
Cash and term deposits	1 389 722	1 009 111	(380 611)	(27)
Cash pool	171 529	35 651	(135 878)	(79)
Unliquidated obligations	1 279 729	657 512	(622 217)	(49)
Reserves and fund balances	277 265	388 070	110 805	40

13. The total income of $162.6 million in 2006-2007, derived mainly from interest earned on cash and term deposits and the cash pool, represented a decrease of 36 per cent from the 2004-2005 figure of $255.8 million. The 36 per cent decrease was primarily attributable to the transfers of funds of $371.1 million made to the Development Fund for Iraq during the biennium 2006-2007 resulting in the consequent decline of interest earned.

14. Total expenditure declined significantly from $421.5 million in 2004-2005 to $118 million in 2006-2007. The decrease of 72 per cent resulted in an excess of income over expenditure of $44.6 million, compared with a deficit of $165.7 million in the preceding biennium.

15. The total cash resources of $1.56 billion in 2005 decreased considerably, by 37 per cent, to $1 billion in 2007. Despite the decline, the cash resources adequately covered the $657.5 million in current and prior period unliquidated obligations arising from approved contracts for humanitarian supplies and oil spares. Total reserves and fund balances increased by 40 per cent, or $111 million, from $277 million in 2005 to $388 million in 2007. The increase was principally brought about by the excess of income over expenditure of $44.6 million and the increase in operating reserves of $60 million.

5. Wind-down and liquidation activities

16. The Administration continued the wind-down and liquidation of the escrow accounts. Arrangements for the liquidation of the outstanding letters of credit carried out in coordination with the Government of Iraq and the designated bank were regularly reported to the Security Council. In his letter dated 8 November 2007 (S/2007/661), the President of the Security Council conveyed the Council members' affirmation that the oil-for-food programme would be terminated by 31 December

2007 and sought the full cooperation of all relevant parties to fulfil their responsibilities.

17. Four months after the declared termination date, however, the liquidation continued to be hampered by the delay in the issuance of authentication documents by the Government of Iraq despite the repeated calls of the Security Council and the Secretary-General. This has unduly extended the termination of the programme, with no definite timetable for resolving all outstanding issues and achieving complete closure. More than four years into the wind-down and liquidation of the programme, the transfer of all surplus funds in the escrow accounts at the earliest possible time to the Development Fund for Iraq, as decided by the Security Council in its resolution 1483 (2003) (para. 17), is yet to be undertaken.

18. The Administration informed the Board that specific targets have been set for the orderly termination of the programme, including: (a) the establishment of the 90-day period within which a letter of credit can be kept current after the expiry; (b) the establishment of a Working Group to try to resolve the issues; and (c) the proposal for a claims settlement mechanism.

19. The Administration also commented that the Secretary-General, through his latest letter dated 9 May 2008 (S/2008/318), had outlined the progress made with respect to the issues involved and that the Security Council, through the letter dated 23 May 2008 from the President of the Council (S/2008/341), had extended the time limit to resolve outstanding issues until 30 June 2008. The Council members had also requested that the Working Group reconvene in June 2008 with a view to receiving an updated report from the Secretary-General in July 2008. The Council members had reaffirmed that they would take the necessary decisions in order to conclude all outstanding issues and end the programme without the possibility of any further extension.

6. United Nations system accounting standards and financial statement disclosures

20. The Board assessed the extent to which the financial statements of the United Nations escrow (Iraq) accounts for the biennium ended 31 December 2007 conformed to the United Nations system accounting standards. The review indicated that the presentation of the financial statements was generally consistent with the standards.

21. In compliance with the recommendation of the Board in its report for the financial year ended 31 December 2006 (S/2007/445), the financial statements were presented in accordance with the liquidation basis of accounting, which may require the realization of assets and extinguishment of liabilities outside the normal course of business. The Administration disclosed in the notes to the financial statements that, as at 31 December 2007, the escrow accounts had no assets or liabilities that required adjustments or reclassification under the liquidation basis of accounting.

7. Accounts and financial reporting

Letters of credit

22. The United Nations Treasury, using the designated bank's liability report, indicated that as at 31 December 2007 there were 210 outstanding letters of credit with an approximate value of $656.3 million, as shown in table 3. The cash collaterals associated with the outstanding letters of credit remain in the United

Nations escrow (Ira_4) accounts until the contracted goods or services are delivered and paid for or the letters of credit are cancelled for non-delivery of the goods or services. All 210 outstanding letters of credit had expired by 31 December 2007.

Table 3
Bank liability report as at 31 December 2007

Expiration date	*Number of letters of credit*	*Value (United States dollars)*
2004	42	53 982 125
2005	10	4 471 712
2006	81	202 940 716
2007	77	394 859 812
Total	**210**	**656 254 366**

Unliquidated obligations

23. The unliquidated obligations are cancelled upon the release of cash collaterals associated with the specific letters of credit. As indicated in paragraph 21 above, there were 210 outstanding letters of credit as at 31 December 2007. Of those, only 164 had claims of delivery, while 46 had no claims. As at 29 February 2008, the number of outstanding letters of credit had been further reduced to 167, consisting of 148 with claims of delivery and 19 without pending claims. The details of these changes are summarized in table 4.

Table 4
Status of letters of credit

	Number of outstanding letters of credit		
	With claims of delivery	*Without pending claims of delivery*	*Total*
Balance as at 31 December 2007	164	46	210
Cancelled letters of credit (January-February 2008)	(13)	(27)	(40)
Fully paid letters of credit (January-February 2008)	(3)	—	(3)
Balance as at 29 February 2008	**148**	**19**	**167**

24. The 19 letters of credit with no pending claims of delivery are further detailed in table 5. None of these letters of credit had extended validity beyond 31 December 2007 and there were no pending documents with the designated bank as at 29 February 2008. Therefore, the associated cash collaterals may be eligible for release and the reversal of the corresponding unliquidated obligations may now be considered.

Table 5
Letters of credit with no claims of delivery of goods and services

Expiration date	*Number of letters of credit*	*Value (United States dollars)*
2004	3	1 292 159
2006	7	47 758 493
2007	9	84 135 303
Total	**19**	**133 185 955**

25. In its reports dated 29 June 2007 (S/2007/445) and 28 July 2006 (S/2006/673), the Board called upon the Administration to coordinate closely with the designated bank for the release of the cash collaterals and to reverse obligations for letters of credit against which no procurement had taken place. The Board noted that prior period obligations amounting to $480 million had been cancelled during the 2006-2007 biennium. However, continuing efforts are needed to finally close the obligations associated with the 19 expired letters of credit without claims of delivery.

26. **The Board recommends that the Administration continue to pursue with the designated bank the review and release of cash collaterals associated with the expired letters of credit with no claims of delivery.**

27. The Administration commented that in a continued effort to move towards the termination of the operations of the programme, the Secretariat continued to regularly review letters of credit that had expired on their own terms with no claims of delivery. As a result of this continued review, the designated bank was able to cancel in March and April 2008 13 of the 19 letters of credit shown in table 5 with no claims of delivery. Accordingly, the corresponding cash collateral was released from the collateral portion to the non-collateral portion of the United Nations escrow (Iraq) accounts and would be available, in principle, for the transfer to the Development Fund for Iraq pursuant to Security Council resolution 1483 (2003). However, 6 of the 19 letters of credit shown in table 5 could not be cancelled by the designated bank as there were outstanding claims of delivery in the bank's files.

8. Processing of authentication documents

28. More than four years after the announcement of the termination of the programme in November 2003, the Secretary-General repeatedly expressed his concern over the chronic problem of the slow provision or non-provision of authentication documents by the Government of Iraq, as set out in his letters to the Security Council between August 2005 and December 2007. In addition, the Secretary-General informed the Council of allegations in 2006 that authentication documents had been improperly withheld by authorities in Iraq, and that payments had been requested from vendors as a condition for authentication.

29. Underlining that the situation could present a serious risk to the timely termination of the programme, the Security Council addressed another letter to the Permanent Representative of Iraq to the United Nations urging the Government of Iraq to do its utmost, in liaison with the Secretariat, to expedite the processing of the

remaining letters of credit in respect of contracts where delivery has been effected (S/2007/661).

9. "Humanitarian activities in Iraq" account

30. In his letter dated 10 July 2006 (S/2006/510), the Secretary-General informed the Security Council that until the issues of claims from suppliers were resolved, the amount of $187 million would be held in a reserve for any unanticipated claims from suppliers, and recalled that the United Nations had no indemnification from the Government of Iraq. The Council took note of the proposed arrangements in a letter dated 14 August 2006 (S/2006/646), and an operating reserve of $187 million was accordingly established under the "Humanitarian activities in Iraq" account. The reserve stood at the same level as at 31 December 2007.

10. "Administrative and operational costs" account

31. An operating reserve of $21.1 million was established as at 31 December 2005 under the "Administrative and operational costs" account to meet the expected costs of the Independent Inquiry Committee and the administrative costs of the United Nations escrow (Iraq) accounts until the programme is fully liquidated. Disbursements amounting to $6.4 million were recorded during the 2006-2007 biennium. An increase in the reserve amounting to $9.7 million in respect of requirements for 2008 was recorded in the same biennium, leaving the reserve at $24.4 million as at 31 December 2007.

11. "Monitoring, verification and inspection" account

32. By its resolution 687 (1991), the Security Council established the United Nations Special Commission to carry out immediate on-site inspection of Iraq's biological, chemical and missile capabilities. Noting that Iraq had not complied with the Council's resolutions 686 (1991) and 687 (1991), the Council, by its resolution 1284 (1999), established the United Nations Monitoring, Verification and Inspection Commission (UNMOVIC), which replaced the Special Commission. UNMOVIC assumed the responsibilities mandated to the Special Commission and took over all of its assets, liabilities and archives. Its costs were met from the funds deposited in an escrow account established under Security Council resolution 986 (1995).

33. By resolution 1762 (2007), the Security Council terminated the mandate of UNMOVIC. An operating reserve of $36 million was established as at 30 June 2007 under the "Monitoring, verification and inspection" account to meet the estimated liquidation costs pertaining to UNMOVIC, including the settlement of debts owed to the Government of Germany and archiving and staff-related costs. During the period from 1 July to 31 December 2007, the reserve was used to settle the debts owed to the Government of Germany of $23.9 million and to make staff-related disbursements of $6.6 million. A sum of $2.5 million was returned to the cumulative surplus, leaving a reserve balance of $3 million as at 31 December 2007. Unencumbered funds in the amount of $65.1 million were transferred to the Development Fund for Iraq on 31 December 2007, and $0.9 million was transferred on 28 February 2008.

12. End-of-service benefits including after-service health insurance

34. Staff members separated from the service are entitled to any unused vacation days up to a maximum of 60 days, repatriation benefits based on the number of years of service and after-service health insurance benefits. The General Assembly, in its resolution 60/255, recognized the end-of-service accrued benefit liabilities reported by the Secretary-General (see A/60/450 and Corr.1) and requested the Secretary-General to take steps to disclose those liabilities in the United Nations financial statements.

35. The Board noted that, for the financial year ended 31 December 2006, the end-of-service benefits were presented as liabilities in the escrow account financial statements. Deviating from this previous practice, however, the end-of-service benefits were excluded from the liability accounts and considered in calculating and establishing the operating reserves in 2007. As at 31 December 2007, the total estimated end-of-service benefits included in the operating reserves of the "Administrative and operational costs" and the "Monitoring, verification and inspection" (UNMOVIC) accounts amounted to US$ 2.6 million and US$ 2.4 million, respectively. These are detailed in table 6 below.

Table 6
End-of-service benefits as at 31 December 2007
(United States dollars)

Benefits	*Administrative and operational costs account*	*Monitoring, verification and inspection account*
Accrued unused vacation days	156 841	336,486
Repatriation grants	307 307	431 967
After-service health insurance	2 148 000	1 643 000
Total	**2 612 148**	**2 411 453**

36. Except for the after-service health insurance under UNMOVIC of $1.6 million, which was transferred and presented as a liability (Fund ASR) in the accounts of the United Nations Headquarters, the end-of-service benefits were, at the instance of the Board, presented as separate line items under operating reserves in the statement of assets, liabilities and reserves and fund balances (statement II) of the escrow accounts.

13. Write-offs and disposals

37. As required by financial rule 106.9, the Administration informed the Board that property losses amounting to $1.4 million were written off during the biennium 2006-2007. The write-off pertained to property losses sustained by UNMOVIC ($1.1 million), and the United Nations Office of the Humanitarian Coordinator for Iraq ($0.3 million), mainly due to hostilities. In addition, properties valued at $5.4 million were disposed off during the biennium.

14. Ex gratia payments

38. In accordance with financial rule 105.12, the Administration reported no ex gratia payments during the biennium 2006-2007.

15. Independent inquiry into the oil-for-food programme

39. In April 2004, the Secretary-General appointed a high-level Independent Inquiry Committee to investigate the administration and management of the oil-for-food programme. Although the work of the Committee was substantially completed in 2005, its term was extended to assist the duly authorized law enforcement and regulatory agencies in cases arising from its work.

40. On 1 January 2007, the Committee wound up its operation and at the same time the Office of the Independent Inquiry Committee was established for an interim period of two years as part of the Secretariat. The work of the Office is being performed by the representative designated by the former members of the Committee and his or her designees. Its costs of $469,000 were met from funds allocated for the administrative and operational costs of the programme. Expenditure during the biennium ended 31 December 2007 amounted to $2.6 million and is detailed in note 4 of the notes to the financial statements.

16. Cases of fraud and presumptive fraud

41. The Administration advised the Board that in two cases, vendors had reported that they had not been paid for goods supplied to Iraq. They cited illegal withholding by the Government of Iraq of the authentication documents necessary to effect payments against the letters of credit.

42. The Board, in its report dated 29 June 2007 (S/2007/445), invited the Administration to keep the Board informed of the outcome of any investigation of the matter. No such information has so far been brought to the attention of the Board.

43. The Board, though, noted that the Secretary-General, in his letter of 25 July 2007 (S/2007/476), had informed the Security Council of the July 2007 agreement with the designated bank, whereby upon the transmittal of the authentication documents to the designated bank by the Central Bank of Iraq, the Secretariat will provide the designated bank with a letter advising that it has conducted a review of the letter-of-credit file to which the authentication document pertains. The letter would further state that it did not identify evidence of allegations that anything of value had been improperly requested from or promised or provided by or on behalf of the beneficiary of the letter of credit in exchange for the issuance of the authentication documents by the Central Bank of Iraq. If the review of a letter-of-credit file identifies such evidence of allegations, the Secretariat will advise the designated bank and the Security Council of such evidence and will request direction from the Security Council as to the appropriate course of action. Pending receipt of such written direction from the Council, the Secretariat will hold the authentication document.

44. The Administration advised the Board that other than those two cases, there were no known cases of fraud or presumptive fraud relating to the activities of the programme.

C. Acknowledgement

45. The Board wishes to express its appreciation for the cooperation and assistance extended to the auditors by the Secretary-General, the Under-Secretary-General for Management, the Assistant Secretary-General and Controller and their staff.

(*Signed*) Philippe **Séguin**
First President of the Court of Accounts of France
(Chairman, United Nations Board of Auditors)

(*Signed*) Reynaldo A. **Villar**
Chairman, Philippine Commission on Audit
(Lead Auditor)

(*Signed*) Terence **Nombembe**
Auditor-General of the Republic of South Africa

30 June 2008

Annex

Summary of the status of implementation of the Board's recommendations for the biennium ended 31 December 2005 and for the financial year ended 31 December 2006

	Summary of recommendation	*Paragraph reference*	*Financial period first made*	*Fully implemented*	*Under implementation*	*Overtaken by events*
Report of the Board of Auditors for the biennium ended 31 December 2005						
1	Strongly urge the Security Council and the Government of Iraq to finally resolve the issue of contracts with expired letters of credit	31 (a)	2002-2003		The Administration continues to update the Security Council on the progress in resolving all outstanding issues in coordination with the Government of Iraq.	
2	Continue to coordinate closely with the designated bank for the release of the cash collateral associated with each expired letter of credit in order to adjust the unliquidated obligations at the time the cash collateral is released by the bank	31 (b)	2002-2003		The Administration is currently pursuing the release of cash collaterals pertaining to expired letters of credit with no claims of delivery.	
3	Initiate evaluation of the UNMOVIC mandate in the light of current events and again invite the Security Council to decide the final course of action to take	46	2004-2005	Security Council resolution 1762 (2007) terminated the mandate of UNMOVIC on 29 June 2007.		
4	Facilitate completion of the final inventory necessary to update the UNMOVIC records of non-expendable property lost or stolen	51	2004-2005			Updating of records continued until the termination of the mandate of UNMOVIC. The bulk of the non-expendable property was either sold, transferred to the Government of Iraq or agencies, written off or disposed of.
Report of the Board of Auditors for the financial year ended 31 December 2006						
5	Prepare the financial statements of the United Nations escrow (Iraq) account covering the final liquidation year in accordance with the liquidation basis of accounting	17	2006	The notes to the 2006-2007 biennium financial statements disclosed that the United Nations escrow (Iraq) accounts were presented in accordance with the liquidation basis of accounting.		

	Summary of recommendation	*Paragraph reference*	*Financial period first made*	*Fully implemented*	*Under implementation*	*Overtaken by events*
6	Reverse the obligations pertaining to letters of credit where parties agreed to their cancellation	23	2006		The Administration has regularly coordinated with the designated bank for the cancellation of expired letters of credit and release of the associated cash collaterals in order to reverse the obligations.	
7	Urge the Government of Iraq to accelerate the processing of authentication documents	25	2006		The Security Council has kept on urging the Government of Iraq to do its utmost, in liaison with the Secretariat, to expedite the processing of authentication documents.	
	Number of recommendations			**2**	**4**	**1**
	Percentage of total number of recommendations			**29**	**57**	**14**

II. Audit opinion

We have audited the accompanying financial statements of the United Nations escrow (Iraq) accounts comprising statements numbered I to III and the supporting notes to the financial statements, for the biennium ended 31 December 2007. These financial statements, which have been prepared according to the liquidation basis of accounting, are the responsibility of the Secretary-General. Our responsibility is to express an opinion on the financial statements based on our audit.

We conducted our audit in accordance with the International Standards on Auditing. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis and as considered by the auditor to be necessary in the circumstances, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting policies used and significant estimates made by the Secretary-General, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for the audit opinion.

In our opinion, the financial statements present fairly, in all material respects, the financial position of the United Nations escrow (Iraq) accounts as at 31 December 2007 and the results of the operations and the cash flows for the period then ended, in accordance with the United Nations system accounting standards.

Furthermore, in our opinion, the transactions of the United Nations escrow (Iraq) accounts that have come to our notice, or which we have tested as part of our audit, have in all significant respects been in accordance with the Financial Regulations and Rules of the United Nations and legislative authority.

In accordance with article VII of the Financial Regulations and Rules of the United Nations, we have also issued a long-form report on our audit of the financial statements of the United Nations escrow (Iraq) accounts.

(*Signed*) Philippe **Séguin**
First President of the Court of Accounts of France
(Chairman, United Nations Board of Auditors)

(*Signed*) Reynaldo A. **Villar**
Chairman, Philippine Commission on Audit
(Lead Auditor)

(*Signed*) Terence **Nombembe**
Auditor-General of the Republic of South Africa

30 June 2008

III. Certification of the financial statements

The financial statements prepared pursuant to Security Council resolutions 687 (1991), 706 (1991), 778 (1992), 986 (1995), 1284 (1999), 1483 (2003) and 1762 (2007) for the biennium ending 31 December 2007 have been prepared in accordance with financial rule 106.10.

The summary of significant accounting policies applied in the preparation of these statements is included as notes to the financial statements. These notes provide additional information and clarifications for the financial activities related to Security Council resolutions 687 (1991), 706 (1991), 778 (1992), 986 (1995), 1284 (1999), 1483 (2003) and 1762 (2007) undertaken by the Organization during the period covered by these statements, for which the Secretary-General has administrative responsibility.

I certify that the appended financial statements of the United Nations escrow (Iraq) accounts, numbered I to III, are correct.

(*Signed*) Warren **Sach**
Assistant Secretary-General, Controller

28 March 2008

IV. Financial statements

Statement I

United Nations escrow accounts established under the provisions of Security Council resolutions relating to Iraq[a]

Statement of income and expenditure and changes in reserves and fund balances for the biennium ended 31 December 2007

(Thousands of United States dollars)

	Resolutions 986 (1995) and 1483 (2003)		*Resolutions 687 (1991), 706 (1991), 1284 (1999), 1762 (2007)[b]*	*Resolutions 687 (1991), 706 (1991)[c]*		
	Humanitarian activities in Iraq	*Administrative and operational costs*	*Monitoring, verification and inspection*	*Other activities*	*Total 2007*	*Total 2005*
Income						
Funding from operating reserves[d]	—	6 368	6 619	—	12 987	37 242
Interest income	90 431	2 710	7 471	—	100 612	166 805
Miscellaneous income	6	1 500	34	1	1 541	51 705
Currency exchange adjustments[e]	47 444	8	—	—	47 452	7
Total income	**137 881**	**10 586**	**14 124**	**1**	**162 592**	**255 759**
Expenditure						
Purchase of humanitarian supplies[f]	86 554	—	—	—	86 554	200 358
Purchase of spare parts[g]	1 701	—	—	—	1 701	79 387
Inter-agency operational expenses	—	—	—	—	—	2 496
Administrative expenses	—	4 262	22 626	246	27 134	59 919
Independent Inquiry Committee expenses[h]	—	2 565	—	—	2 565	35 854
Currency exchange adjustments[e]	—	—	—	—	—	43 478
Total expenditure	**88 255**	**6 827**	**22 626**	**246**	**117 954**	**421 492**
Excess (shortfall) of income over expenditure	**49 626**	**3 759**	**(8 502)**	**(245)**	**44 638**	**(165 733)**
Prior-period adjustments	(2 443)[i]	—	(23 888)[i]	—	(26 331)	(5)
Net excess (shortfall) of income over expenditure	**47 183**	**3 759**	**(32 390)**	**(245)**	**18 307**	**(165 738)**
Savings on/or cancellation of prior-period obligations	479 999	69	270	1	480 339	1 677 903
Transfers to Development Fund for Iraq[k]	(306 000)	—	(65 105)	—	(371 105)	(4 440 322)

	Resolutions 986 (1995) and 1483 (2003)		*Resolutions 687 (1991), 706 (1991), 1284 (1999), 1762 (2007)*[b]	*Resolutions 687 (1991), 706 (1991)*[c]		
	Humanitarian activities in Iraq	*Administrative and operational costs*	*Monitoring, verification and inspection*	*Other activities*	*Total 2007*	*Total 2005*
Transfers to the United Nations and other entities[i]	—	—	(3 749)	—	(3 749)	(22 712)
Transfer from operating reserves[d]	—	(6 368)	(6 619)	—	(12 987)	(37 242)
Reserves and fund balances, beginning of period	135 781	27 173	113 928	383	277 265	3 265 376
Reserves and fund balances, end of period	**356 963**	**24 633**	**6 335**	**139**	**388 070**	**277 265**

[a] There were no activities relating to pipelines tariff charges and assets transfers and contributions during this period; see also notes 1 and 3.
[b] Refers to the United Nations Monitoring Verification and Inspection Commission; see note 3.
[c] Refers to activities undertaken further to Security Council resolutions 687 (1991) and 706 (1991); see note 3.
[d] See note 5.
[e] Represents currency exchange fluctuations between the euro and the United States dollar and other currencies.
[f] Expenditure incurred during the biennium 2006-2007 for humanitarian supplies relates to adjustments and reinstatements of contracts entered into in previous years. The figure includes unliquidated obligations of $83,389,319.
[g] Expenditure incurred during the biennium 2006-2007 for spare parts relates to adjustments and reinstatements of contracts entered into in previous years.
[h] See note 4.
[i] Represents reimbursement to UN-Habitat for its prior-period expenditures.
[j] Represents reimbursement effected pursuant to Security Council resolution 1762 (2007), para. 6, to the Government of Germany for services provided to the United Nations Special Commission of $24,467,670 less $579,267 that had been previously provided for.
[k] Represents transfers to the Development Fund for Iraq held by the Central Bank of Iraq pursuant to Security Council resolution 1483 (2003); see notes 7 (e) and 7 (f).
[l] Represents transfers of $416,871 and $772,234 to the United Nations and $2,560,238 (€1,874,094) to the United Nations Industrial Development Organization for payment of outstanding assessed contributions of the Government of Iraq.

The accompanying notes are an integral part of the financial statements.

Statement II

United Nations escrow accounts established under the provisions of Security Council resolutions relating to Iraq[a]

Statement of assets, liabilities and reserves and fund balances as at 31 December 2007

(Thousands of United States dollars)

	Resolutions 986 (1995) and 1483 (2003)		*Resolutions 687 (1991), 706 (1991), 1284 (1999), 1762 (2007)*	*Resolutions 687 (1991), 706 (1991)*		
	Humanitarian activities in Iraq	*Administrative and operational costs*	*Monitoring, verification and inspection*	*Other activities*	*Total 2007*	*Total 2005*
Assets						
Cash and term deposits	1 009 089	13	9	—	1 009 111	1 389 722
Cash pool	—	25 517[b]	10 134[c]	—	35 651	171 529
Accounts receivable						
Inter-fund balances receivable[d]	—	—	—	139	139	367
Inter-agency accounts receivable[e]	4 624	—	—	—	4 624	5 312
Other accounts receivable	105	44	30	2	181	2 716
Deferred charges	—	7	11	—	18	40
Total assets	**1 013 818**	**25 581**	**10 184**	**141**	**1 049 724**	**1 569 686**
Liabilities						
Unliquidated obligations — current year	83 389[f]	459	214	1	84 063	105 750
Unliquidated obligations — prior years	573 449[g]	—	—	—	573 449	1 173 979
Accounts payable						
Inter-fund balances payable[d]	17	315	3 520	—	3 852	11 528
Inter-agency accounts payable	—	—	—	—	—	90
Other accounts payable	—	174	115	1	290	1 073
Inter-office transactions pending processing	—	—	—	—	—	1
Total liabilities	**656 855**	**948**	**3 849**	**2**	**661 654**	**1 292 421**
Reserves and fund balances						
Operating reserves[h]						
Reserves for end-of-service and post-retirement benefits	—	2 612	768	—	3 380	—

	Resolutions 986 (1995) and 1483 (2003)		*Resolutions 687 (1991), 706 (1991), 1284 (1999), 1762 (2007)*	*Resolutions 687 (1991), 706 (1991)*		
	Humanitarian activities in Iraq	*Administrative and operational costs*	*Monitoring, verification and inspection*	*Other activities*	*Total 2007*	*Total 2005*
Other reserves	187 000	21 822	2 221	—	211 043	147 792
Cumulative surplus	169 963	199	3 346	139	173 647	129 473
Total reserves and fund balances	**356 963**	**24 633**	**6 335**	**139**	**388 070**	**277 265**
Total liabilities and reserves and fund balances	**1 013 818**	**25 581**	**10 184**	**141**	**1 049 724**	**1 569 686**

[a] There were no activities relating to pipelines tariff charges and assets transfers and contributions during this period; see also notes 1 and 3.

[b] Represents the share of the United Nations Headquarters cash pool for "Administrative and operational costs", comprising cash and term deposits of $9,049,983, short-term investments of $5,080,314 (market value $5,082,941), long-term investments of $11,235,523 (market value $11,269,877) and accrued interest receivable of $151,023.

[c] Represents share of the United Nations Headquarters cash pool for "Monitoring, verification and inspection", comprising cash and term deposits of $3,594,175, short-term investments of $2,017,632 (market value $2,018,675), long-term investments of $4,462,156 (market value $4,475,799) and accrued interest receivable of $59,979.

[d] See note 2 (k) (iv).

[e] Represents the funds advanced to the United Nations agencies for the implementation of humanitarian activities.

[f] Unliquidated obligations incurred during the biennium 2006-2007 for humanitarian supplies and spare parts relates to adjustments and reinstatements of contracts entered into in previous years.

[g] See note 7 (d).

[h] See note 5.

The accompanying notes are an integral part of the financial statements.

Statement III

United Nations escrow accounts established under the provisions of Security Council resolutions relating to Iraq[a]

Statement of cash flows for the biennium ending 31 December 2007

(Thousands of United States dollars)

	Resolutions 986 (1995) and 1483 (2003)		*Resolutions 687 (1991), 706 (1991), 1284 (1999), 1762 (2007)*	*Resolutions 687 (1991), 706 (1991)*		
	Humanitarian activities in Iraq	*Administrative and operational costs*	*Monitoring, verification and inspection*	*Other activities*	*Total 2007*	*Total 2005*
Cash flows from operating activities						
Net excess (shortfall) of income over expenditure (statement I)	47 183	3 759	(32 390)	(245)	18 307	(165 738)
(Increase) decrease in inter-fund balances receivable	—	—	—	228	228	2 310
(Increase) decrease in inter-agency accounts receivable	212	121	355	—	688	65 268
(Increase) decrease in other accounts receivable	1 969	159	381	26	2 535	8 657
(Increase) decrease in other assets	—	—	—	—	—	264
(Increase) decrease in deferred charges	—	8	14	—	22	3 209
Increase (decrease) in unliquidated obligations	(620 880)	(1 199)	(136)	(2)	(622 217)	(6 492 342)
Increase (decrease) in inter-fund accounts payable	(197)	(10 532)	3 053	—	(7 676)	5 777
Increase (decrease) in inter-agency accounts payable	—	—	(90)	—	(90)	(52 797)
Increase (decrease) in other accounts payable	—	(139)	(636)	(8)	(783)	(3 519)
Increase (decrease) in inter-office transactions pending processing	—	(1)	—	—	(1)	(84)
Less: Interest income	(90 431)	(2 710)	(7 471)	—	(100 612)	(166 805)
Net cash from operating activities	**(662 144)**	**(10 534)**	**(36 920)**	**(1)**	**(709 599)**	**(6 795 800)**
Cash flows from investing activities						
(Increase) decrease in cash pool	17 154	14 093	104 631	—	135 878	1 269 442
Plus: interest income	90 431	2 710	7 471	—	100 612	166 805
Net cash from investing activities	**107 585**	**16 803**	**112 102**	**—**	**236 490**	**1 436 247**
Cash flows from financing activities						
Savings on or cancellation of prior-period obligations	479 999	69	270	1	480 339	1 677 903

	Resolutions 986 (1995) and 1483 (2003)		*Resolutions 687 (1991), 706 (1991), 1284 (1999), 1762 (2007)*	*Resolutions 687 (1991), 706 (1991)*		
	Humanitarian activities in Iraq	*Administrative and operational costs*	*Monitoring, verification and inspection*	*Other activities*	*Total 2007*	*Total 2005*
Transfers to the Development Fund for Iraq	(306 000)	—	(65 105)	—	(371 105)	(4 440 322)
Transfers to the United Nations and other entities	—	—	(3 749)	—	(3 749)	(22 712)
Transfer from operating reserves	—	(6 368)	(6 619)	—	(12 987)	(37 242)
Net cash from financing activities	**173 999**	**(6 299)**	**(75 203)**	**1**	**92 498**	**(2 822 373)**
Net increase (decrease) in cash and term deposits	**(380 560)**	**(30)**	**(21)**	—	**(380 611)**	**(8 181 926)**
Cash and term deposits, beginning of period	**1 389 649**	**43**	**30**	—	**1 389 722**	**9 571 648**
Cash and term deposits, end of period	**1 009 089**	**13**	**9**	—	**1 009 111**	**1 389 722**

[a] There were no activities relating to pipelines tariff charges and assets transfers and contributions during this period; see also notes 1 and 3.

The accompanying notes are an integral part of the financial statements.

Notes to the financial statements

Note 1
United Nations escrow account established under the provisions of Security Council resolution 986 (1995) (statements I, II and III)

(a) An escrow account to be administered by the Secretary-General was established in 1996 in order to receive the proceeds from the sale of Iraqi oil approved by Security Council resolution 986 (1995). The Council, in paragraph 1 of that resolution, authorized States to permit the import of petroleum and petroleum products originating in Iraq, including financial and other essential transactions directly relating thereto, sufficient to produce a sum not exceeding a total of $1 billion every 90 days. In paragraph 3 of that resolution the Council decided that the provision should remain in force for 180 days.

(b) The authorization given in paragraph 2 of resolution 986 (1995) permitted Turkey to import petroleum and petroleum products originating in Iraq, sufficient to meet the pipeline tariff charges for the transport of these products through the Kirkuk-Yumurtalik pipeline in Turkey, after the deduction of 30 per cent for the Compensation Fund. By resolution 1330 (2000) the Council revised this deduction to 25 per cent. Owing to the cessation of the oil-for-food programme, pipeline tariff charges are no longer incurred.

(c) The provision of resolution 986 (1995) authorizing sales of Iraqi oil not exceeding a total of $1 billion every 90 days remained in force until 30 May 1998 by virtue of resolutions 1111 (1997), 1129 (1997), 1143 (1997) and 1158 (1998).

(d) The Security Council, in paragraph 2 of resolution 1153 (1998), which took effect on 1 June 1998, decided that the authorization given to States by paragraph 1 of resolution 986 (1995) should permit the import of petroleum and petroleum products originating in Iraq, including financial and other essential transactions directly relating thereto, sufficient to produce a sum not exceeding a total of $5.256 billion, in the 180-day period referred to in paragraph 1 of resolution 1153 (1998). This provision remained in force in accordance with resolutions 1210 (1998), 1242 (1999) and 1281 (1999).

(e) By resolution 1284 (1999) of 17 December 1999, the Council lifted the dollar cap and authorized sales of Iraqi oil of any volume during the 180-day mandate period. This provision remained in force until 3 June 2003 by virtue of resolutions 1302 (2000), 1330 (2000), 1352 (2001), 1360 (2001), 1382 (2001), 1409 (2002), 1443 (2002) and 1447 (2002). The final sale of oil under the programme was for shipment made on 20 March 2003.

(f) The Security Council, in paragraphs 1 and 3 of resolution 1175 (1998), authorized States to permit the export to Iraq of the necessary parts and equipment to enable Iraq to increase the export of petroleum and petroleum products in quantities sufficient to produce the sum established in paragraph 2 of resolution 1153 (1998), and decided that the funds in the escrow account produced pursuant to resolution 1153 (1998), up to a total of $300 million, might be used to meet any reasonable expenses, other than expenses payable in Iraq, which follow directly from contracts approved by the Committee established by resolution 661 (1990). Resolutions 1293 (2000) and 1302 (2000) established that up to $600 million might be used to permit States to export to Iraq the necessary parts and equipment to

enable Iraq to increase the export of petroleum and petroleum products. Resolutions 1330 (2000), 1352 (2001), 1360 (2001), 1382 (2001), 1409 (2002) and 1447 (2002) retained the $600 million limit.

(g) Resolution 1330 (2000) allowed for funds up to €600 million from the escrow account to be used for the installation and maintenance, including training services, of spare parts and equipment relating to the oil industry.

(h) In its resolution 1472 (2003) of 28 March 2003, the Security Council recognized that in view of the exceptional circumstances prevailing in Iraq, on an interim and exceptional basis, technical and temporary adjustments should be made to the programme, and authorized the Secretary-General to make such changes for a period of 45 days.

(i) In its resolution 1476 (2003) of 24 April 2003, the Security Council decided that the provisions contained in paragraph 4 of resolution 1472 (2003) should remain in force until 3 June 2003 and might be subject to further renewal by the Council.

(j) In its resolution 1483 (2003) of 22 May 2003, the Security Council requested the Secretary-General to terminate the programme within six months and to transfer responsibility for the administration of any remaining activity to the Coalition Provisional Authority. The Council also requested the consolidation of the accounts established pursuant to paragraphs 8 (a) (relating to 15 governorates of central and southern Iraq) and 8 (b) (relating to 3 governorates of northern Iraq) of resolution 986 (1995).

(k) The sale of Iraqi oil is recognized as revenue in the fund for humanitarian activities in Iraq based on the bill of lading date and the total value of oil loaded as stipulated in the commercial invoice issued by the State Oil Marketing Organization. The proceeds from sales of Iraqi oil are allocated, upon receipt of deposits, to other accounts established pursuant to paragraph 8 of resolution 986 (1995). No oil sales have been recorded since 20 March 2003.

(l) The funds from the sale of Iraqi oil pursuant to the authorization given in paragraph 1 of resolution 986 (1995) are to be used to meet the humanitarian needs of the Iraqi people and for the other purposes set out in paragraph 8 of resolution 986 (1995). Resolution 1409 (2002) permits the sale or supply of any commodities or products other than those referred to in paragraph 24 of resolution 698 (1991) as it relates to military commodities and products, or military-related commodities or products covered by the Good Review List (S/2002/515) and the amendments thereto specified in resolution 1454 (2002). The percentages used in allocating the oil sale proceeds were determined as follows:

(i) 53.034 per cent to finance the export to Iraq of medicines, health supplies, food and materials and supplies for essential civilian needs. By resolution 1302 (2000) this was increased to 54.034 per cent and by resolution 1330 (2000) to 59.034 per cent, less the payment referred to in (vi) below;

(ii) 13 per cent to complement the distribution by the Government of Iraq of goods imported by providing funds to the United Nations Inter-Agency Humanitarian Programme operating in the three northern governorates of Iraq, Arbil, Dihouk and Suleimaniyeh;

(iii) 2.215 per cent to meet the operational and administrative costs of the United Nations;

(iv) 30 per cent allocated to the Compensation Fund established by Security Council resolution 705 (1991). Pursuant to resolution 1330 (2000) this was decreased to 25.0 per cent;

(v) 0.751 per cent allocated to the United Nations Monitoring, Verification and Inspection Commission established by Security Council resolution 1284 (1999), which replaced the Special Commission established by Security Council resolution 687 (1991), to meet operating costs;

(vi) A maximum of $10 million dollars every 90-day period to be allocated to the escrow account established by Security Council resolutions 706 (1991) and 712 (1991) for the payments envisaged under paragraph 6 of resolution 778 (1992). Resolution 1284 (1999) suspended payments to this escrow account for an initial period of six months from 17 December 1999. Resolution 1302 (2000) extended this suspension for a further 180-day period and transferred the allocation to (i) above. Resolution 1330 (2000) reinstated the allocation of a maximum of $10 million every 90 days from 6 December 2000.

(m) Notwithstanding the periods for the sale of Iraqi oil as authorized by the Security Council, financial statements I, II and III (United Nations escrow accounts) are prepared every six months.

(n) Included in financial statements I, II and III are details relating to the humanitarian activities, and related operational and administrative costs, that are undertaken under the provisions of Security Council resolution 986 (1995). From the beginning of the programme in December 1996 to mid-2000, implementation costs on actual expenditures incurred by agencies for activities associated with the purchase of humanitarian goods for northern Iraq were charged to the "Humanitarian activities in Iraq" account, and programme support costs on actual expenditures for the administrative and operational costs were charged to the "Administrative and operational costs" account. In mid-2000, following recommendations of the Board of Auditors, and taking into account the increased level of funds available in the "Administrative and operational costs" account, the Secretariat decided to prospectively charge all implementation and programme support costs to the "Administrative and operational costs" account. In mid-2002, the Secretariat reverted to the earlier practice, whereby direct costs of implementing the programme in northern Iraq were charged to the "Humanitarian activities in Iraq" account. This decision reflected the need to harmonize the practice, whether the work was done by an agency itself or contracted out. In 2003, when agencies began implementing various aspects of the programme in southern/central Iraq, those implementation costs were also charged to the "Humanitarian Activities in Iraq" account, in line with the 2002 decision.

(o) The financial statements of the Compensation Fund (see paragraph (l) (v) above) are reported on in a separate volume of the United Nations financial statements.

(p) Expenditure incurred during the biennium 2006-2007 for humanitarian supplies and spare parts relates to adjustments and reinstatements of contracts entered into in previous years.

Note 2
Summary of significant accounting and financial reporting policies of the United Nations

(a) The accounts of the United Nations are maintained in accordance with the Financial Regulations and Rules of the United Nations adopted by the General Assembly, the rules formulated by the Secretary-General as required under the regulations, and administrative instructions issued by the Under-Secretary-General for Management, or the Controller. They also take fully into account the United Nations system accounting standards adopted by the United Nations System Chief Executives Board for Coordination. The Organization follows International Accounting Standard 1, "presentation of financial statements", on the disclosure of accounting policies, as modified and adopted by the United Nations System Chief Executives Board for Coordination, as shown below:

(i) Going concern, consistency, and accrual are fundamental accounting assumptions. Where fundamental accounting assumptions are followed in financial statements, disclosure of such assumptions is not required. If a fundamental accounting assumption is not followed, that fact should be disclosed together with the reasons (see note 3 (a) below);

(ii) Prudence, substance over form, and materiality should govern the selection and application of accounting policies;

(iii) Financial statements should include clear and concise disclosure of all significant accounting policies that have been used;

(iv) The disclosure of the significant accounting policies used should be an integral part of the financial statements. These policies should normally be disclosed in one place;

(v) Financial statements should show comparative figures for the corresponding period of the preceding financial period;

(vi) A change in an accounting policy that has a material effect in the current period or may have a material effect in subsequent periods should be disclosed together with the reasons. The effect of the change should, if material, be disclosed and quantified.

(b) The Organization's accounts are maintained on a fund accounting basis. Separate funds for general or special purposes may be established by the General Assembly, the Security Council or the Secretary-General. Each fund is maintained as a distinct financial and accounting entity with a separate self-balancing double-entry group of accounts. Separate financial statements are prepared for each fund or for a group of funds of the same nature.

(c) The financial period of the Organization is a biennium and consists of two consecutive calendar years for all funds other than peacekeeping accounts, which are reported on a fiscal year basis covering the period from 1 July to 30 June.

(d) Generally, income, expenditure, assets and liabilities are recognized on the accrual basis of accounting.

(e) The accounts of the Organization are presented in United States dollars. Accounts maintained in other currencies are translated into United States dollars at the time of the transactions at rates of exchange established by the United Nations.

In respect of such currencies, the financial statements shall reflect the cash, investments, unpaid pledges and current accounts receivable and payable in currencies other than the United States dollar, translated at the applicable United Nations rates of exchange in effect at the date of the statements. In the event that the application of actual exchange rates at the date of the statements would provide a valuation materially different from the application of the Organization's rates of exchange for the last month of the financial period, a footnote will be provided quantifying the difference.

(f) The Organization's financial statements are prepared on the historical cost basis of accounting and are not adjusted to reflect the effects of changing prices for goods and services.

(g) The cash flow summary statement is based on the indirect method of cash flows as referred to in the United Nations system accounting standards.

(h) The Organization's financial statements are presented in accordance with the ongoing recommendations of the Task Force on Accounting Standards to the High Level Committee on Management.

(i) Income:

(i) Voluntary contributions from Member States or other donors are recorded as income on the basis of a written commitment to pay monetary contributions at specified times within the current financial period. Voluntary contributions made in the form of services and supplies that are acceptable to the Secretary-General are credited to income or noted in the financial statements;

(ii) Income received under inter-organizational arrangements represents allocations of funding from agencies to enable the Organization to administer projects or other programmes on their behalf;

(iii) Allocations from other funds represent monies appropriated or designated from one fund for transfer to and disbursement from another fund;

(iv) Income for services rendered include amounts charged for salaries of staff members and other costs which are attributable to providing technical and administrative support to other organizations;

(v) Interest income includes all interest earned on deposits in various bank accounts, investment income earned on marketable securities and other negotiable instruments, and investment income earned in the cash pool. All realized losses and net unrealized losses on short-term investments are offset against investment income. Investment income and costs associated with operation of investments in the cash pool are allocated to participating funds. Interest income is available for allotment purposes on a six-monthly basis;

(vi) Net gains or losses on currency fluctuations other than for the current year's obligations are accumulated on a six-monthly basis. Effective 1 January 2002, the net amount is recognized as income or expenditure every six months in the financial statements;

(vii) Miscellaneous income includes income from the rental of premises, the sale of used or surplus property, refunds of expenditures charged to prior periods, settlements of insurance claims, monies accepted for which no purpose was specified, and other sundry income;

(viii) Income relating to future financial periods is not recognized in the current financial period and is recorded as deferred income (see item l (iii) below).

(j) Expenditure:

(i) Expenditures are incurred against authorized appropriations or commitment authorities. Total expenditures reported include unliquidated obligations and disbursements. Expenditures also include currency exchange adjustments arising from the evaluation of current-period obligations;

(ii) Expenditures incurred for non-expendable property are charged to the budget of the period when acquired and are not capitalized. Inventory of such non-expendable property is maintained at historical cost;

(iii) Expenditures for future financial periods are not charged to the current financial period and are recorded as deferred charges (see item k (vi) below).

(k) Assets:

(i) Cash and term deposits represent funds in demand deposit accounts and interest bearing bank deposits;

(ii) Investments include marketable securities and other negotiable instruments acquired by the Organization to produce income. Short-term investments are stated at the lower of cost or market value; long-term investments are stated at cost. Cost is defined as the nominal value plus/minus any unamortized premium/discount. The market value of investments is disclosed in the footnotes to the financial statements;

(iii) Cash pools comprise participating funds' share of the cash and term deposits, short-term and long-term investments and accrual of investment income, all of which are managed in the cash pools. The investments in the cash pools are similar in nature. Short-term investments are stated at the lower of cost or market value; long-term investments are stated at cost. Cost is defined as the nominal value plus or minus any unamortized premium or discount. The share in cash pools is reported separately in each of the participating fund's statement and its composition and the market value of its investments are disclosed in footnotes in the individual statements;

(iv) Inter-fund balances reflect transactions between funds and are included in the amounts due to and from the United Nations General Fund. Inter-fund balances also reflect transactions directly with other escrow accounts and with the United Nations General Fund. Inter-fund balances are settled periodically, depending on the availability of cash resources;

(v) Provision for delays in collection of receivable balances is not made;

(vi) Deferred charges normally comprise expenditure items that are not properly chargeable in the current financial period. They will be charged as expenditure in a subsequent period. These expenditure items include commitments approved by the Controller for future financial periods in accordance with financial rule 106.7. Such commitments are normally restricted to administrative requirements of a continuing nature and to contracts or legal obligations where long lead-times are required for delivery;

(vii) For purposes of the balance sheet statements only, those portions of education grant advances that are assumed to pertain to the scholastic years completed as at the date of the financial statement are shown as deferred charges. The full amounts of the advances are maintained as accounts receivable from staff members until the required proofs of entitlement are produced, at which time the budgetary accounts are charged and the advances settled;

(viii) Maintenance and repairs of capital assets are charged against the appropriate budgetary accounts. Furniture, equipment, other non-expendable property, and leasehold improvements are not included in the assets of the Organization. Such acquisitions are charged against budgetary accounts in the year of purchase. The value of non-expendable property is disclosed in notes to the financial statements.

(l) Liabilities and reserves and fund balances:

(i) Operating reserves are included in the totals for reserves and fund balances shown in the financial statements;

(ii) Unliquidated obligations for future years are reported both as deferred charges and as unliquidated obligations;

(iii) Deferred income includes income received but not yet earned;

(iv) Commitments of the Organization relating to prior, current, and future financial periods are shown as unliquidated obligations. Effective 1 January 2000, unliquidated obligations for the escrow account for humanitarian activities in Iraq remain valid until completion of the project. All other obligations continue to remain valid for 12 months following the end of the biennium to which they relate;

(v) Contingent liabilities, if any, are disclosed in the notes to the financial statements;

(vi) The United Nations is a member organization participating in the United Nations Joint Staff Pension Fund which was established by the General Assembly to provide retirement, death, disability and related benefits. The Fund is a funded defined benefit plan. The financial obligation of the Organization to the Fund consists of its mandated contribution at the rate established by the General Assembly together with its share of any actuarial deficiency payments under article 26 of the Regulations of the Fund. Such deficiency payments are only payable if and when the General Assembly has invoked the provision of article 26, following a determination that there is a requirement for deficiency payments based on an assessment of the actuarial sufficiency of the Fund as of the valuation date. As at the date of the current financial statement, the General Assembly has not invoked this provision.

Note 3
United Nations escrow accounts established under the provisions of Security Council resolutions 687 (1991), 706 (1991), 778 (1992) and 1284 (1999) (statements I, II and III)

(a) As the United Nations escrow account is in the liquidation process (see note 7 below), the going concern assumption is not followed and the financial

statements are presented according to the liquidation basis of accounting, which may require realization of assets and extinguishment of liabilities outside the normal course of business. As at 31 December 2007, the escrow account had no assets or liabilities requiring adjustments in their measurement or classification under the liquidation basis of accounting;

(b) Included in financial statements I, II and III are the escrow accounts established pursuant to Security Council resolutions 706 (1991) and 712 (1991) for the payments envisaged under paragraph 6 of resolution 778 (1992), and the special account established pursuant to resolutions 687 (1991), 706 (1991) and 1284 (1999). The escrow account established under resolutions 706 (1991), 712 (1991) and 778 (1992) returned all funds in 2003. As a result there are no further transactions to report relating to this escrow account.

(c) The escrow account administered by the Secretary-General under Security Council resolutions 706 (1991) and 712 (1991) provided for Iraqi funds from the sale of oil to be used for payment by the United Nations Compensation Commission, the full costs of carrying out the tasks authorized by section C of resolution 687 (1991), the full costs incurred by the United Nations in facilitating the return of all Kuwaiti property seized by Iraq, half the costs of the Boundary Commission, and the cost to the United Nations of implementing resolution 706 (1991), and of other necessary humanitarian activities in Iraq:

(i) With the refusal of Iraq to sell oil under the provisions of Security Council resolutions 706 (1991) and 712 (1991), the Security Council adopted resolution 778 (1992) on 2 October 1992 as an alternate means of providing funds for the purposes specified. States in which there were petroleum products owned by Iraq or States in which there were funds of the Government of Iraq representing the proceeds of petroleum sales, paid for by the purchaser after 6 August 1990, were required to transfer some or all of these funds to the escrow account. Additionally, in resolution 778 (1992) the Council urged States to contribute funds from other sources to the escrow account. All such funds transferred or contributed to the escrow account under the provisions of resolution 778 (1992) were to be transferred back to the accounts of States from which funds had been provided, together with applicable interest, at such time when oil exports had taken place pursuant to the system provided for in resolutions 706 (1991) and 712 (1991) and the escrow account had received funds from the proceeds of sale. Iraqi oil exports began in December 1996 and in January 1997 the escrow account started receiving funds from the proceeds of sale that were transferred back to the accounts of States that had provided the original funds to the escrow account.

(ii) In December 1999, pursuant to Security Council resolution 1284 (1999), payment to the escrow account from the proceeds of sale was suspended. The suspension, which was extended for an additional 180 days by Security Council resolution 1302 (2000), was lifted by resolution 1330 (2000) in December 2000.

(iii) In May 2003, the Security Council, in its resolution 1483 (2003), requested the Secretary-General to restore funds that had been provided by Member States pursuant to resolution 778 (1992). All such funds were returned in June 2003.

(d) The Security Council, in its resolution 687 (1991), requested the Secretary-General to undertake certain tasks in connection with the situation between Iraq and Kuwait. The costs of those activities were to be considered as an advance pending the receipt of payments to the Organization by Iraq in respect of certain activities and by Iraq and Kuwait jointly in respect of the costs of the Boundary Commission:

(i) Since the adoption by the Security Council of resolution 778 (1992), the above-mentioned costs have been covered by transfers from the escrow account. Furthermore, the costs of the Special Commission are met by transfer from the escrow account pursuant to Security Council resolution 986 (1995);

(ii) The Security Council decided by resolution 1284 (1999) to establish UNMOVIC. The responsibilities mandated to the Special Commission are undertaken by UNMOVIC;

(iii) In its resolutions 1483 (2003) and 1546 (2004), the Council reaffirmed its intention to revisit the mandate of UNMOVIC;

(iv) By its resolution 1762 (2007), the Security Council terminated the mandate of UNMOVIC and requested the Secretary-General to transfer all remaining unencumbered funds to the Government of Iraq within three months, after returning to Member States at their request contributions made by them pursuant to paragraph 4 of resolution 699 (1991).

Note 4
Independent Inquiry Committee into the United Nations oil-for-food programme

(a) In April 2004, the Secretary-General appointed a high-level Independent Inquiry Committee to investigate the administration and management of the oil-for-food programme from its inception to its transfer to the Coalition Provincial Authority, including allegations of fraud and corruption on the part of United Nations officials, personnel and agents as well as contractors, including entities that had entered into contracts with the United Nations or with Iraq under the programme. By its resolution 1538 (2004) of 21 April 2004, the Security Council welcomed the inquiry. The Independent Inquiry Committee completed its investigation and on 27 October 2005 issued its final report.

(b) Effective 1 January 2007, the Independent Inquiry Committee wound up its operation and the Office of the Independent Inquiry Committee was established for an interim period of two years as part of the Secretariat. During this period, the work of the Office is being performed by the representative designated by the former members of the Committee and his or her designees.

(c) The costs of the Independent Inquiry Committee were met from funds allocated for the administrative and operational costs of the programme. Expenditures during the biennium 2006-2007 ending 31 December 2007 were as follows (in thousands of United States dollars):

Salaries	1 088.1
Consulting fees	758.1
Travel	107.3
Audit fees	75.0
Communication	64.6
Premises	442.9
Equipment	21.6
Miscellaneous supplies and services	7.4
Local transportation	0.3
Total	**2 565.3**

Note 5
Operating reserves

"Humanitarian activities in Iraq" account

(a) An operating reserve of $126,660,000 was established as of 31 December 2005 under the "Humanitarian activities in Iraq" account to ensure that sufficient funds are available for the satisfactory resolution of all remaining issues relating to outstanding letters of credit. In a letter dated 10 July 2006 (S/2006/510), the Secretary-General, recalling that the United Nations had no indemnification from the Government of Iraq on the funds that had been transferred to date to the Development Fund of Iraq, informed the Security Council that until the issues of claims from suppliers were resolved, and if there was no objection from the Council, an amount of $187 million would be held on reserve for any unanticipated claims from suppliers. The Council took note of the proposed arrangements in its letter dated 14 August 2006 (S/2006/646), and an operating reserve of $187 million was established.

"Administrative and operational costs" account

(b) An operating reserve of $21,132,192 was established as of 31 December 2005 under the "Administrative and operational costs" account to meet the expected costs of the Independent Inquiry Committee and the administrative costs of the escrow accounts until all aspects of the programme are completed. Disbursements amounting to $6,367,856 were recorded during the period from 1 January 2006 to 31 December 2007, while an increase amounting to $9,669,664 in respect of requirements for 2008 was recorded, leaving the reserve at a level of $24,434,000 as of 31 December 2007. This amount is shown on two separate lines of operating reserves in statement II above; $2,612,148 is for end-of-service and post-retirement benefits and the remaining $21,821,852 is for other purposes. Operating reserves for end-of-service and post-retirement benefits comprised $156,841 for unused vacation days, $307,307 for repatriation benefits and $2,148,000 for after-service health insurance benefits.

"Monitoring, verification and inspection" account

(c) An operating reserve of $35,958,863 was established as of 30 June 2007 under the "Monitoring, verification and inspection" account to meet the estimated

liquidation costs pertaining to UNMOVIC, including the settlement of debts owed to the Government of Germany and archiving and staff-related costs. Staff-related costs include accrued liabilities for end-of-service and after-service benefits. During the period from 1 July to 31 December 2007, the reserve was used to settle the debts owed to the Government of Germany of $23,888,403 and for staff-related disbursements of $6,618,333, which included after-service health insurance benefits of $1,643,000. A sum of $2,462,927 was returned to the cumulative surplus, leaving the reserve at a level of $2,989,200 as of 31 December 2007. This amount is shown on two separate lines of operating reserves in statement II; $768,453 is for end-of-service benefits and the remaining amount of $2,220,747 is for other purposes. Operating reserves for end-of-service benefits comprised $336,486 for unused vacation days and $431,967 for repatriation benefits.

(d) Contingent liabilities described in note 8 shall be met to the extent necessary from operating reserves of the programme.

Note 6
Non-expendable property

In accordance with United Nations accounting policies, non-expendable property is charged against the current allotment in the year of purchase. The non-expendable property valued at historical cost, according to the cumulative inventory records, is shown below (in thousands of United States dollars):

	2007	*2005*
UNMOVIC	1 262	11 242
Agencies[a]	1 093	4 570
Independent Inquiry Committee	315	1 022

[a] Owing to the current situation in Iraq, it is not possible to fully ascertain the value of non-expendable property in Iraq as at 31 December 2007.

Note 7
Future modus operandi of United Nations escrow accounts established under Security Council resolutions 986 (1995) and 1284 (1999)

(a) In its resolution 1483 (2003) of 22 May 2003, the Security Council extended the Secretary-General's responsibilities under Security Council resolutions 1472 (2003) and 1476 (2003) for a period of six months. The Council requested the Secretary-General to terminate, in the most cost effective manner, the ongoing operations of the programme, both at Headquarters and in the field, by 21 November 2003, and to transfer responsibility for the administration of any remaining activity under the programme to the Authority.

(b) Accordingly, in the three governorates of northern Iraq where the United Nations agencies were implementing the programme, contracts entered into by the agencies were transferred to the Authority. Similarly, in the 15 governorates of central and southern Iraq where, after the outbreak of hostilities, agencies had been assigned responsibility for procurement activities previously undertaken by the Government of Iraq, uncompleted contracts were handed over to the Authority.

(c) By its resolution 1546 (2004), the Security Council decided that in connection with the dissolution of the Authority, the Interim Government of Iraq and its successors should assume the rights, responsibilities and obligations relating to the programme that had been transferred to the Authority, including all operational responsibility for the programme and any obligations undertaken by the Authority in connection with such responsibility, and responsibility for ensuring independently authenticated confirmation that goods had been delivered, and further decided that, following a 120-day transition period from the date of adoption of the resolution, the Interim Government of Iraq and its successors should assume responsibility for certifying delivery of goods under previously prioritized contracts, and that such certification should be deemed to constitute the independent authentication required for the release of funds associated with such contracts, consulting as appropriate to ensure the smooth implementation of those arrangements.

(d) As of 31 March 2008, the liquidation of the programme continued. All obligations relating to contracts that had not been prioritized in accordance with Security Council resolution 1483 (2003) had been closed, except for those where letters of credit had not lapsed. Obligations relating to contracts that had been prioritized remain as liabilities of the programme, and the related letters of credit have not been closed. The expiry dates for the letters of credit extend until 2007. In his letters dated 8 August 2005, 17 October 2005, 19 December 2005, 10 July 2006, 8 December 2006, 27 March 2007, 9 April 2007, 25 July 2007 and 7 December 2007, the Secretary-General kept the Security Council informed of the arrangements for the liquidation of the outstanding letters of credit, and of the slow progress being made. Through his letter dated 7 December 2007, the Secretary-General, inter alia, updated the Council on the extension and/or reinstatement of specific letters of credit; the submission to BNP Paribas (the designated bank) of all the necessary documents related to the 17 letters of credit included in annex VI to the letter dated 25 July 2007; and the proposals to address unresolved issues including the establishment of mechanisms to deal with outstanding issues.

(e) The representatives of the Secretary-General and the Government of Iraq met from 7 to 17 January 2008 to discuss arrangements for the cancellation or retention of letters of credit. It was agreed that 57 letters of credit with an approximate value of $183 million could, if the Security Council had no objection, be cancelled. The Secretary-General, in his letter of 11 March 2008, informed the Council that 17 letters of credit (with an approximate value of about $140 million) out of the 57 targeted for cancellation had not been cancelled, as the bank was still performing its due diligence. The Secretariat has since been informed by the bank that 14 of those, with an approximate value of $137 million, have claims of delivery and therefore cannot be cancelled.

(f) By its resolution 1762 (2007), the Security Council terminated the mandate of UNMOVIC, pursuant to which an operating reserve to meet liquidation costs was established (see note 5) and unencumbered funds in the amount of $25,104,523 were transferred to the Development Fund for Iraq on 28 September 2007; a further sum of $875,285 was transferred on 28 February 2008.

(g) From the adoption of Security Council resolution 1483 (2003) up to 31 December 2007, a total of $10.41 billion has been transferred to the Development Fund for Iraq. This amount includes $371,104,523 transferred during the biennium 2006-2007. The remaining surplus funds will be transferred to the

Development Fund for Iraq in accordance with the provisions of Security Council resolutions 1483 (2003) and 1546 (2004) and such guidance as the Council may provide.

Note 8
Contingent liabilities

Under the terms of Security Council resolution 1483 (2003), as part of the liquidation process, all claims and disputes involving the United Nations or its agencies with third parties in carrying out the activities of the programme are to be transferred to, and become the responsibility of, the Authority, which has since been succeeded by the Government of Iraq. There may be some circumstances where such a transfer is not possible and any liability and related fees will need to be met from operating reserves of the programme (see note 5). Such contingent liabilities include a claim of $4.6 million, which is currently under arbitration with one of the specialized agencies of the United Nations involved in implementation of the programme.